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No. 87-978

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

SHELL OFFSHORE INC., *et al.*,
Petitioners,

v.

ASSOCIATED GAS DISTRIBUTORS, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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PETITIONERS' REPLY BRIEF

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PETITIONERS' REPLY BRIEF

At base, the petition for a writ of certiorari in this docket (the "Producers' Petition"[1]) seeks review of a purely legal question of critical importance: Does the Federal Energy Regulatory Commission ("FERC" or the "Commission") have the statutory authority to abrogate producer-pipeline natural gas contracts merely because they contain take-or-pay provisions? For the most part, the briefs in opposition to the Producers' Petition do not contest the appropriateness of Court review of this issue. Instead, they stress arguments for postponing such review, all of which are without merit.

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[1] Petition for Certiorari, *Shell Offshore Inc. v. Associated Gas Distribs.*, No. 87-978 (filed Dec. 14, 1987). This petition was filed jointly by 21 natural gas producers.

1. FERC concluded in Order No. 436 that it lacked authority to modify or abrogate take-or-pay contracts, noting that proponents had advanced "[n]either the legal nor factual basis for . . . voiding . . . freely negotiated contracts." *See* Order No. 436, 50 Fed. Reg. 42408, 42423-24, 42433-34 (1985) (27a-28a, 55a-57a).[2] The Commission stressed the congressional determination in the Natural Gas Policy Act, 15 U.S.C. §§ 3301-3342, 42 U.S.C. § 7255 (1982) ("NGPA"), that pricing arrangements at the wellhead should be governed by market forces, Order No. 436, 50 Fed. Reg. at 42423 (26a-28a), and found that agency abrogation of producer-pipeline contracts would "raise extremely serious questions regarding the ability of private parties in the gas production industry to rely on private contracts as a tool for structuring basic economic relationships." *Id.* at 42423 (27a). As the court of appeals conceded, action that "essentially substitute[s] FERC price controls for the wellhead market [is] . . . clearly forbidden by the NGPA." *Associated Gas Distribs. v. FERC*, 824 F.2d 981, 1022 n.26 (D.C. Cir. 1987) (P.A. 79a).[3]

FERC also rejected arguments "that the Commission has the authority to require producers to waive contractual rights under the take-or-pay provisions of existing contracts as a condition to obtaining non-discriminatory transportation." Order No. 436, 50 Fed. Reg. at 42433 (55a). The Commission concluded that it would be unduly discriminatory under section 5 of the Natural Gas Act ("NGA"), 15 U.S.C. § 717d (1982), to deny pipeline access to producers merely because they decline to

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[2] Parenthetical references following citations to Order No. 436 are to page numbers in the Appendix submitted with the Brief in Opposition of Exxon Corporation and Conoco Inc. to the petitions for certiorari filed in Docket Nos. 87-976, 87-977, 87-979.

[3] References following citations to the decision below, *Associated Gas Distribs. v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), are to the Appendix filed with the Producers' Petition and are designated "P.A."

forfeit contract rights. Order No. 436-A, 50 Fed. Reg. 52217, 52226 (1985). Refusal to provide transportation services in such circumstances "would discriminate not only against the producer-seller, but also against the willing buyer who has never been a party to the take-or-pay contract in the first place." *Id.* FERC believed, moreover, that with respect to nonjurisdictional gas (*i.e.*, gas not subject to regulation under the NGA), conditioning producer access in this fashion would have the effect of coercing producers "to take action which is beyond our power to compel." Order No. 436, 50 Fed. Reg. at 42433 (56a). For all of these statutory reasons, FERC declined "by essentially a stroke of the pen, to void thousands of gas purchase agreements nationwide and to declare worthless some $7 billion worth of contract damage claims." *Id.* at 42423 (27a).

On appeal, the D.C. Circuit, seemingly ignoring the Commission's statutory analysis on the point, ordered FERC to "reassess" its refusal to invoke its authority under NGA section 5 to set aside contracts with "troublesome" take-or-pay provisions. *See Associated Gas*, 824 F.2d at 1027-28 (P.A. 89a-91a). Further, the court explicitly rejected FERC's conclusion that it lacked authority to condition producer access to pipelines on the waiving of take-or-pay contract provisions, declaring that the relevant statutes pose "no barrier" to such agency action. *Id.* at 1030 (P.A. 94a). In so ruling, the court of appeals erred by failing to acknowledge "that considerable weight should be accorded to [FERC's] construction of [the] statutory scheme," and it impermissibly "substitute[d] its own [statutory] construction . . . for [the] reasonable interpretation made by" FERC. *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984).[4]

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[4] Contrary to the assertion of Tennessee Gas Pipeline Co. (Tenn. Gas. Opp. at 9 n.16), FERC's counsel has not "repudiated" the agency's view that it lacks statutory authority to abrogate take-or-

The opposition brief of Associated Gas Distributors, *et al.* ("AGD"), urges that the question presented is "unripe" for review under *Abbott Laboratories v. Gardner*, 387 U.S. 136, 148-49 (1967). (*See* AGD Opp. at 9.) But *Abbott* speaks only to the finality of administrative agency orders. Before the D.C. Circuit, the AGD group's arguments against FERC's statutory construction on the take-or-pay issue conceded the finality of Order No. 436, as do the separate pending certiorari petitions seeking review of other issues raised by that same FERC order.[5]

Equally unfounded is the contention by Tennessee Gas Pipeline Co. and AGD that when a court of appeals vacates an agency's determination on a point of statutory interpretation and remands the matter for further proceedings consistent with the appellate court's reading of the statute, it is premature for this Court to review the statutory construction question. (Tenn. Gas Opp. at 8-9; AGD Opp. at 9.) To the contrary, this Court has routinely reviewed statutory interpretation questions in just such circumstances. *See, e.g., Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29 (1983);

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pay contracts. Counsel merely argued that the agency's decision not to require contract abrogation could be upheld on other grounds. In any event, counsel's *post hoc* statements cannot supplant the rationale of the agency as set forth in Order No. 436. *See, e.g., Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168-69 (1962); *SEC v. Chenery Corp.*, 318 U.S. 80, 87 (1943).

[5] Most of these petitions seek review of the question whether FERC is empowered to require nondiscriminatory pipeline access as a condition to authorizing certain transportation services. *See* Petitions for Certiorari, *Interstate Natural Gas Ass'n of America v. FERC*, No. 87-976 (filed Dec. 14, 1987); *Texas Eastern Transmission Corp. v. FERC*, No. 87-977 (filed Dec. 14, 1987); *City of Willcox, Arizona v. FERC*, No. 87-979 (filed Dec. 14, 1987). The assertion that this issue is ripe for review while the contract-abrogation question is not (*see* Tenn. Gas Opp. at 7) defies logic, since both issues arise from the same FERC order.

EPA v. National Crushed Stone Ass'n, 449 U.S. 64 (1980); *Southern Ry. Co. v. Seaboard Allied Mining Corp.*, 442 U.S. 444 (1979); *FCC v. National Citizens Comm. for Broadcasting*, 436 U.S. 775 (1978); *Vermont Yankee Nuclear Power Corp. v. Natural Resources Defense Council, Inc.*, 435 U.S. 519 (1978).

2. Although the Solicitor General does not join the argument that this Court is somehow barred from reviewing the contract-abrogation authority issue at this juncture, his opposition suggests that "the propriety" of whatever take-or-pay contract-abrogation policy FERC adopts on remand "may be considered in review proceedings following the Commission's decision." (S.G. Opp. at 27.) This observation reflects a misperception of the legal issue presented for review. That issue is whether the Commission has authority to abrogate producer-pipeline contracts (either by direct intervention or by requiring producers to waive contract rights as a condition of pipeline access), a question not open to further consideration by the Commission on remand. The Solicitor General's assertion that "the Commission might reaffirm its decision regarding the take-or-pay issue" (*id.* at 27 n.18) thus evades the question. The relevant point here is that in view of the D.C. Circuit's decision, FERC is not free to decline to order take-or-pay relief on the ground that it lacks authority to do so.[6] Without ques-

[6] Not surprisingly, shortly after the D.C. Circuit's decision, FERC issued an interim order (No. 500) which is already having the effect of abrogating take-or-pay contracts. Order No. 500, 52 Fed. Reg. 30334, 30338-41 (1987). FERC correctly reads the D.C. Circuit decision as establishing the existence of contract-abrogation authority and, correctly or incorrectly, as requiring FERC to exercise this authority immediately. The Commission has stated that "it has an *obligation* under *AGD* and related court orders to implement the interim procedures for [abrogating] take-or-pay" contracts. Order No. 500-C, 52 Fed. Reg. 48986, 48990 (1987) (emphasis added). In the view of FERC Commissioner Sousa, the D.C. Circuit has "stated in essence that open access transportation *should be* condi-

tion, the D.C. Circuit's ruling on the contract-abrogation issue "is fundamental to the further conduct of" proceedings in this area, and as such, that aspect of the decision below warrants immediate review by this Court. *United States v. General Motors Corp.*, 323 U.S. 373, 377 (1945). *See also Gillespie v. United States Steel Corp.*, 379 U.S. 148, 153 (1964); *Land v. Dollar*, 330 U.S. 731, 734 n.2 (1947).

3. The assertion by Tennessee Gas that NGPA section 601(c)(1), 15 U.S.C. § 3431(c)(1) (1982), is "irrelevant" to the question whether FERC may condition producer access to pipelines on the waiving of take-or-pay contract provisions ignores the readily apparent meaning of the statute. (*See* Tenn. Gas. Opp. at 14.) Section 601(c)(1) was intended to prevent the Commission from attempting to do indirectly what it is prohibited from doing directly—interfering with the wellhead pricing of natural gas. *See Office of Consumers' Counsel v. FERC*, 783 F.2d 206, 221 (D.C. Cir. 1986) (NGPA legislative history indicates a concern with prohibiting "back door" regulation of producers). Under section 601(c)(1), the Commission "may not deny, or condition the grant of, any certificate" based on the amount to be paid so long as the price is "just and reasonable," 15 U.S.C. § 3431(c)(1) (1982), and in this case, the pricing provisions of the take-or-pay contracts are by statutory definition "just and reasonable."[7] The court of appeals conceded that its fundamental concern was that the freely negotiated take-or-pay contracts "provide for prices far in

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tioned on take-or-pay [contract-abrogation] relief" and, by issuing the mandate putting into effect the *AGD* decision below, has "approved" the contract-abrogation provisions already adopted by FERC in Order No. 500. Order No. 500-B, 52 Fed. Reg. 39630, 39633 (1987) (emphasis added).

[7] *See* NGPA § 601(b)(1)(A), 15 U.S.C. § 3431(b)(1)(A) (1982) (except in circumstances not relevant here, pricing provisions in producer-pipeline contracts "shall be deemed to be just and reasonable").

excess of current market levels." *Associated Gas*, 824 F.2d at 1021 (P.A. 75a). The conditioning of transportation access on producers' agreeing to abrogate those contracts is thus directly violative of section 601(c)(1)'s prohibition on pricing-based conditioning by FERC.[8]

4. The Court also has before it petitions for certiorari seeking review of the question whether FERC is empowered to require nondiscriminatory pipeline access as a condition to the authorization of certain transportation services. *See* p. 4 n.5 *supra*. The court of appeals correctly deferred to FERC's well-reasoned statutory analysis on this question, and review by this Court is not warranted.[9] Should this Court decide to review the nondiscriminatory access question, however, prompt review of the contract-abrogation issue would become even more critical. Both FERC and the D.C. Circuit held that the nondiscriminatory access issue could not be considered without simultaneous consideration of the contract-abrogation issue. *See* Order No. 436, 50 Fed. Reg. at 42422 (23a) (the issues are "inextricably related"); *Associated Gas*, 824 F.2d at 1044 (P.A. 124a) ("[t]he parts of Order No. 436 are interdependent"). Similarly, Petitioners respectfully submit that this Court should not address FERC's authority to impose the nondiscriminatory access condition as a means of furthering the goals of the NGA and NGPA without also determining whether the court of appeals' decision granting FERC authority to abrogate gas contracts undermines those very same statutes and their purposes.

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[8] Contrary to the contention of one opposition brief (Tenn. Gas Opp. at 14), Order No. 436 explicitly notes the substantive limits on FERC's authority imposed by NGPA section 601(c)(1). *See* Order No. 436, 50 Fed. Reg. at 42423 (28a) .

[9] *See* Oppositions to Petitions for Certiorari filed by Shell Offshore Inc. *et al.* (dated Feb. 19, 1988) and by Exxon Corporation and Conoco Inc. (dated Mar. 16, 1988) in Docket Nos. 87-976, 87-977, and 87-979.

For all of the foregoing reasons, a writ of certiorari should issue.

Respectfully submitted,

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